

**THE IMPACT OF THE FUTURE FREE TRADE AGREEMENT
BETWEEN THE EUROPEAN UNION AND SOUTH KOREA
ON THE EUROPEAN AND ROMANIAN ECONOMIES
– A MARKETING RESEARCH –**

Iacob CĂTOIU, Tudor EDU
Academy of Economic Studies, Bucharest

Abstract. *The signing of a Free Trade Agreement between South Korea and the European Union is one of the main goals of the General Affairs and External Relations Council of the EU. The FTA between the EU and South Korea will have a significant impact on the European economy with positive and negative consequences. The goal of this study is to determine the opportunities and possible threats for the European and Romanian economies. The most important effects of this Free Trade Agreement could be summarized in the increase of productivity and efficiency and spreading of innovation within a great number of industries.*

Keywords: Free Trade Agreement, EU, South Korea.

Introduction

The signing of a Free Trade Agreement (FTA) between South Korea and the European Union is one of the main goals of the General Affairs and External Relations Council of the EU. This Council plans to negotiate free trade agreements with South Korea, India, ASEAN, the Andean Community and the Central American Common Market. The European Union is concerned with the creation of a new multilateral framework of free trade compatible with the provisions established within the World Trade Organization by approaching the uncovered areas such as: investment, trade in certain services and removal of non-tariff barriers.

The FTA between the European Union and South Korea will have a significant impact on the European economy with positive and negative consequences. This is why the identification of the opportunities and threats brought about could be considered a must for the European companies and, especially, for the Romanian ones. In this regard we consider that a marketing research of the secondary data pertaining to the ongoing negotiations and reactions of the parties involved could clarify several aspects of the unknown implications of this agreement.

The goal of this study is to determine the opportunities and possible threats of the future Free Trade Agreement between the European Union and South Korea for the European and Romanian economies.

The main objectives of this research could be structured as follows:

1. Evaluation of the status of the bilateral relations prior to the commencement of the negotiations for the Free Trade Agreement;
2. Identification of the areas to be approached in the negotiations for the Free Trade Agreement;

3. Determination of the main measures and decisions which will define the future Free Trade Agreement;

4. Identification of the potential main effects caused by the implementation of the Free Trade Agreement.

The research method used to reach the objectives is the analysis of secondary data, meaning studies of independent bodies; official reports of both sides (the European Union and South Korea); press articles; web sites.

These sources will be investigated to obtain suitable information and to cross-check the correctness of these various sources.

Amongst the plenty of the identified information sources we selected a few considered to be the most comprising.¹

Objective no. 1 – Evaluation of the status of the bilateral relations prior to the commencement of the negotiations for the Free Trade Agreement

The European Union is the second trading partner of South Korea after China with a total value of trade of 79.4 bln. USD in 2007. South Korea is the 8th trading partner of the European Union. The balance of trade has a surplus for South Korea.

The average import tariff rate in the European Union is 4.2% but a higher one is imposed to the most important South Korean exports, such as: automobiles, textiles and electronics. The average import tariff rate imposed by South Korea is 11.2%.

The European Union exports food and beverages worth 1bln. Euro annually, the most important ones being pork and wines.

The European Unions says that the access on the South Korean automobile market is very restrictive for the foreign companies.

The European Union companies encounter difficulties on the pharmaceutical market because the Ministry of Health and Welfare refuses to insure some drugs manufactured in Europe.

At present the trade relations with the European Union are perceived by the South Koreans in a far better way than the ones with the US because of the anti-American feelings induced by the military presence and because the American side desires a greater opening of the food and agricultural markets for the American farmers which would determine great resentment from the South Korean ones. A suitable example in this regard is the „beef” issue of this year.

The European Union is favourably perceived by the South Koreans because of the support offered during the Asian financial crisis in 1997 through the important investments made by the European multinationals in the local companies.

¹ See Annex 1.

Statistics of the trade between the European Union and South Korea by SITC
(Standard International Trade Classification) Section

– main categories of products –

– 2007 –

Products (SITC Sections)	European Union-Imports from South Korea (Mil. Euro)	European Union-Exports to South Korea (Mil. Euro)	Balance of Trade (Mil. Euro)
Machinery and transport equipment	15.929	8.790	-7.139
Manuf. goods classif. chiefly by material	4.147	2.885	-1.262
Miscell. manuf. articles	1.630	2.512	882
Chemicals and related prod., n.e.s	1.526	4.001	2.475
Crude materials inedible, except fuels	380	814	434
Mineral fuels, lubricants and rel. Materials	235	64	-171
Commodit. and transactions n.e.c	174	428	254
Food and live animals	106	702	596
Beverages and tobacco	13	338	325
Animal and vegetable oils, fats and waxes	1	70	69
Total	39.481	24.793	-14.688

Source: Eurostat.

As it can be noticed from the above table, even though the balance of trade is favourable to South Korea, there are categories of products where the value of the European Union exports exceeds the one of the imports. The EU records a deficit in the „Machinery and transport equipment” category because of the automobile imports and of the restrictive access on the South Korean automobile market for the European companies. The EU records deficits also in the following categories: „Manuf. goods classif. chiefly by material” and „Mineral fuels, lubricants and rel. Materials”. The most favourable situations for the European Union are recorded in the „Chemicals and related prod., n.e.s” category and in food, beverages, tobacco and oils. Agriculture is one of the most sensitive topics in the negotiations of the FTA, the South Korean side expressing concerns about the possible negative impact of the reduction of the tariffs and the removal of the non-tariff barriers on farmers.

**The dynamics of the main imports of the European Union from South Korea
2003-2007 (Mil. Euro)**

Product Groups SITC Rev. 3	2003	%	2005	%	2007	%
Total	26,003	100	34451	100	39481	100
Primary Products of which:	437	1.7	764	2.2	868	2.2
Agricultural prod.	139	0.5	105	0.3	135	0.3
Energy	47	0.2	356	1.0	235	0.6
Manuf. Products of which:	25,438	97.8	33,538	97.4	23,099	58.5
Machinery	13,116	50.4	18,899	54.9	6,056	15.3
Transport equipment of which:	7,442	28.6	9,255	26.9	9,873	25.0
<i>Automotive prod.</i>	4,385	16.9	6,742	19.6	7,205	18.2
Chemicals	1,023	3.9	1,158	3.4	1,526	3.9
Textiles and cloth.	1,509	5.8	1,038	3.0	824	2.1

Source: Eurostat.

As it can be noticed, the total value of imports from South Korea increased between 2003-2007; with 32.48% between 2003-2005 and with 14.6% between 2005-2007. In absolute value, the chemical products and transport equipment registered a steady growth. The other categories recorded both increases and decreases during this period of time

**The dynamics of the main exports of the European Union to South Korea
2003-2007 (Mil. Euro)**

Product Groups SITC Rev. 3	2003	%	2005	%	2007	%
Total	16,449	100	20,226	100	24,793	100
Primary Products of which:	1,471	8.9	1,843	9.1	2,441	9.8
Agricultural prod.	869	5.3	1,076	5.3	1,221	4.9
Energy	71	0.4	30	0.1	64	0.3
Manuf. Products of which:	14,457	87.9	17,741	87.7	17,735	71.5
Machinery	5,723	34.8	6,524	32.3	6,112	24.7
Transport equipment of which:	1,725	10.5	2,202	10.9	2,608	10.5
<i>Automotive prod.</i>	1,039	6.3	1,341	6.6	1,432	5.8
Chemicals	2,596	15.8	3,250	16.1	4,001	16.1
Textiles and cloth.	695	4.2	617	3.0	671	2.7

Source: Eurostat.

The impact of the future free trade agreement between the European Union and South Korea

The exports from the European Union to South Korea increased continuously between 2003-2007; with 22.96% between 2003-2005 and with 22.57% between 2005-2007. The agricultural products, the transport equipment (even automobiles) and the chemical products recorded a steady growth in absolute value. The other categories of products registered both increases and decreases in absolute value. The primary products recorded a steady growth in the overall exports as well.

The Trade in services between the European Union and South Korea between 2003-2005

Year	Imports from South Korea (Bn. Euro)	Exports to South Korea (Bn. Euro)	Balance of trade in services (Bn. Euro)
2003	3.4	5.6	2.2
2004	3.6	5.8	2.2
2005	4.0	6.4	2.4

Source: Eurostat.

The balance of trade in services has a positive value for the European Union. The trade in services registered a steady increase from both sides, but the surplus remained approximately at the same level.

The Foreign Direct Investment (FDI) between the European Union and South Korea

Year	FDI in the EU (Bn. Euro)	FDI in South Korea (Bn. Euro)	Balance of FDI (Bn. Euro)
2004	1.4	2.0	0.6
2005	1.3	5.0	3.7
2006	1.0	1.3	0.3

Source: Eurostat.

The balance of Foreign Direct Investment between the two sides is favourable to the European Union. The European investments are favourably perceived in South Korea due to the positive image built during the Asian financial crisis.

It can be concluded that the two economies have a great degree of overlapping. Both of them trade, mainly, products of the same categories. Also, these economies are developed and focus on strengthening their positions on the international arena. They signed FTAs with other countries and organisations and initiated several negotiations for other ones.

Objective no. 2 – Identification of the areas to be approached in the negotiations for the Free Trade Agreement

A comprehensive classification of the areas, which must be approached in this FTA, should include:

1. Economic area-including the following divisions:
 - Labour market;
 - Agricultural markets;
 - Industrial markets-especially heavy machinery and auto, electronics, chemicals, pharmaceuticals;
 - Services;
 - Competition;
 - Intellectual Property Rights;
 - Government purchases;
 - Direct investment;
 - Innovation;
2. Social area- including the following:
 - mutations in the labour structure;
 - employment and unemployment;
 - income distribution;
 - population aging;
 - relocation of labour force;
 - education;
3. Environment – including the following:
 - pollution;
 - natural resources;
 - energy consumption;
 - impact of transportation;
 - proliferation of clean technologies.

Objective no. 3 – Determination of the main measures and decisions which will define the future Free Trade Agreement

The main measures and decisions with an important impact on the future relations between the two sides could be grouped as follows:

1. *Measures related to the policies of the Free Trade Agreement:*
 - the two sides agreed to remove tariffs for 95% of all products and for all industrial products within 10 years;

- if the reduction/removal of tariffs will take place as agreed, the most effects will be encountered in the automobile industry and in agriculture;
- the tariffs for industrial products will be removed and those for agricultural products will be reduced with 40%;
- the reduction of the trade barriers for environmental goods and services, wines and beverages and pharmaceuticals should be considered a top priority for the European Union;

2. Rules of Origin:

- South Korea could express concerns regarding the imports from countries outside the EU with which it has Most Favourite Nation agreements; these imports are absolutely necessary in the automobile industry, textiles and apparel, most of them becoming parts of end-products which are exported;

3. Sanitary and Phytosanitary measures. Technical regulations and Standards:

- the most important areas which will be regulated regarding sanitary and phytosanitary measures, technical regulations and standards are: automobiles, food, electronics and cosmetics.

Specialists belonging to both sides consider at least the following measures as being necessary:

- international relevant standards for sanitary and phytosanitary measures and technical regulations must be used as extensively as possible;
- transparency should be the main goal in the development and enforcement of technical regulations and standards;
- the registration procedures for the suppliers regarding the sanitary and phytosanitary measures should be a common endeavour. Also, the two sides should develop protocols for the implementation of measures, such as: recognition of disease and pest free areas and mutual recognition of the procedures and certificates of conformity;
- both sides should consider mutual recognition of the conformity evaluation and accreditation procedures;
- the dispute settlement procedures should comply with the WTO regulations.

4. Intellectual Property Rights:

- more drastic conditions than the ones provided by the TRIPS Agreement of the WTO and international conventions should be considered.

The TRIPS Agreement enhances the existent international conventions about Intellectual Property Rights (IPR) and its provisions are applied to the following types of IPRs:

- patents;
- copyrights;
- trademarks and service marks;

- industrial designs;
- geographic indications;
- layout designs of integrated circuits;
- trade secrets and know how;
- anti-competitive practices in contractual licenses.

The agreement provides for consultations between governments where there is reason to believe that licensing practices or conditions pertaining to intellectual property rights represent an abuse of these rights and have an adverse effect on competition.

5. Investment:

- there should be more transparency in the limits and control of the European and South Korean investors' level of participation in a company; also these limits should be reduced;
- a common log of restrictive activities should be created, especially in the financial field.

6. Sustainable development:

- due to the convergence of the two economies and of the approximately similar level of economic, social and environmental development, the main objective should be the protection of the environment and the development of clean technologies.

Objective no. 4 – Identification of the potential main effects caused by the implementation of the Free Trade Agreement

Commencing with the idea that the two sides have open economies and are well integrated in the world economy, the effects of the FTA are forecasted to be equally shared. Also, due to the fact that South Korea has become a developed economy and the two economies have a great degree of overlapping and complementarity in goods and services, it can be concluded that there are future opportunities for intra-industrial specialization, scale effect, competitive effects (the reduction/removal of the tariffs will lead to a more competitive environment especially on the most protected markets), investment and innovative effects.

The potential effects of this Free Trade Agreement could be grouped in three main categories: economic effects, social effects and environmental effects.

Economic effects

The main economic effects could be grouped as follows:

Agriculture

The big winner in this case will be the European Union even though the South Korean side will request protection measures for different markets and the EU will have to negotiate drastically. There will be a significant increase in the European

exports of pork and poultry, dairy products, as well as wines and alcoholic beverages (especially whisky). In some cases, pork and poultry can be with 60% less expensive than the local products. In case of alcoholic beverages, the South Korean side levies taxes between 20 and 30% which will disappear once the FTA comes into force. The European dairy products have a significant position on the South Korean market. For example, the European milk powder has a market share of approximately 30% and the European cheese around 10%.

Industry

For South Korea, the most significant gains will be encountered in automobiles, electronics, mobile telephones, textiles and rubber. For the European Union, even with a more flexible framework regarding the automobile market, the predictions show a limited growth of the market share for the European manufacturers. The same predictions apply for electric machinery as well. Also, the iron and steel industries will develop much faster in South Korea than in the European Union.

For the European Union, the biggest gains will come from the following industries: heavy machinery, precision equipment and chemicals. The EU is very interested a greater opening of the South Korean pharmaceutical market. If the negotiations result in less restrictive authorization conditions for the European drugs, the European companies will increase their market shares significantly.

Services

The liberalization of services will bring a significant gain for the European Union, because many South Korean services are very protected through high tariffs or non-tariff barriers.

Estimates show export increases of European services in the following sectors: wholesale and retail trade, transportation, communication, finance and banking, as well as other areas. This growth is estimated to be around 40-60% because of the serious demand of such services from the South Korean side to support the economic development and because of the lack of competition brought about by the high level of protection mainly through non-tariff barriers.

Investment

The investment between the two sides will increase significantly. At present, the European Union is the number one investor in South Korea. There is a big difference between the negotiations for trade and those for investment. In case of trade, each side tries to gain as much as possible regarding market penetration and protection of the local companies. With investment, both sides are interested to increase the foreign direct investment made in respective countries. This is why the rounds of negotiation will be less and shorter than the ones for trade.

The Intellectual Property Rights, Rules of Origin and Technical Standards are essential instruments which will influence the development of agriculture, industry

and services. Both sides will try to gain as much as possible regarding these instruments and the negotiations will be long-lasting.

The labour market will be influenced in size and structure. As it was mentioned before, some industries will develop even at a fast pace, while others will stagnate or even regress. As a whole, the number of jobs will increase in both sides, which will reduce the pressure on unemployment. There will be structural changes within some industries as well.

Social effects

The main social effects could be grouped as follows:

- estimates show an increase in the demand for some professional specialties and a decrease in others;
- there will be an increase in the participation of women in the economy of South Korea;
- there will be a reduction in the structural unemployment in some social and economic groups;
- regarding income distribution, there is a convergence in the purchasing power and income distribution. However there are considerable variations in the EU amongst its members;
- on the long run, both sides must deal with the challenges of high productivity and employment trying to sustain economic growth with a stable and aging population.

Conclusions

The implementation of the FTA does not presume at a first glance adverse effects on the environment because it states that the use of natural resources must be rational and the production growth must be planned considering the impact on the environment.

The only problems foreseen at this moment, with a potential impact on the environment, could be caused by the increase of energy consumption related to the increased production and transportation.

The agreement will lead to the proliferation of clean technologies through increased investment in this area and through a better management of the Intellectual Property Rights.

The most important effects of this Free Trade Agreement could be summarized in the increase of productivity and efficiency and spreading of innovation within a great number of industries. These effects will help the two sides overcoming the social challenges brought about by a stable and aging population and will help them address the opportunities and threats of the global environment.

There is no doubt that this agreement will lead to a growth in the bilateral trade as well as an increase in the inbound and outbound investment. It is to be seen how well the business environment in each part will be able to take advantage of the new framework.

At present, Romania has a significant trade deficit with South Korea even though the exports almost doubled in 2007 related to 2006 (in 2006 the exports amounted to 22.47 mil. Euro and the imports reached 447.08 mil. Euro; in 2007 the Romanian exports equalled 43.23 mil. Euro and the imports 604.74 mil. Euro)².

The Romanian companies should study the South Korean import trend, especially the imports coming from the European Union, in order to identify the main areas of interest on these markets. Also these companies should investigate other sources of information in order to be able to adapt their offerings to the peculiarities of each South Korean market.

The Romanian business environment should pay close attention to the rounds of negotiation of the two sides in order to have a proactive position by communicating to the Romanian authorities different points of view which might stimulate the growth of the Romanian exports to South Korea. Also, the investment side of the negotiations should be closely scrutinized by the business environment and authorities, the main concern being the increase of the South Korean foreign direct investment in Romania.

References

- Trade Sustainability Impact Assessment of the EU-Korea FTA: Draft Final Report- IBM Belgium in association with DMI, Ticon, & TAC- March 2008
- EU Trade Commissioner Peter Mandelson's remarks to the European Parliament on the EU-Korea FTA negotiations on December 13, 2007 in Strasbourg
- EUROPEAN AND SOUTH KOREAN SOCIAL MOVEMENTS AND CIVIL SOCIETY UNITE AGAINST THE 'GLOBAL EUROPE' STRATEGY AND THE SOUTH KOREA-EU FTA- Brussels, 19 September 2007- statement of the South Korean Alliance against Korea-EU FTA (KoA) and of members from social movements and civil society organisations from Europe
- National interests need to be top priority in Korea-EU FTA- 12.05.2007, The Hankyoreh, Seoul- <http://english.hani.co.kr>
- South Korea, EU to wrap up first week of free trade talks- 11.05.2007, Yonhap News- <http://english.yonhapnews.co.kr/engnews>
- FTA with EU to hurt South Korea's alcohol, meat, dairy sectors: report- 07.05.2007, Yonhap News- <http://english.yonhapnews.co.kr/engnews>

² Source: www.dce.gov.ro, accessed September 10th, 2008.

- Korea-EU FTA Talks Get Official Go Ahead- EU Gives Green Light to Trade Talks With Korea- www.chosun.com, May 2007
- Economic Impact of a Potential Free Trade Agreement (FTA) between the European Union and South Korea- short study by Copenhagen Economics & Prof. J. F. Francois- <http://trade.ec.europa.eu/doclib/html/134017.htm>, March 2007
- A special luncheon hosted by The European Union Chamber of Commerce Korea in downtown Seoul on July 4, 2006 to explain the advantages and disadvantages of a Korea-EU FTA
- KIM (KIEP) Heungchong- Korea-EU FTA: Prospects for the Future- *Presented at the Second Italian-South Korean Economic Workshop "Economic Policies, Growth and Economic Integration East Asia and Europe in Perspective" Turin, Fondazione „Luigi Einaudi” - 20 June 2005*